



Investment Management Division

Investment Beliefs

FRAME OF REFERENCE

The ASRS has developed the following *Investment Beliefs* in order to ensure the development of congruent and synergistic investment strategies, and to ensure the effective and efficient allocation of resources.

These *Investment Beliefs* determine the general paradigm within which investment strategies are developed, investment ideas are reviewed, and investment decisions are implemented.

Modifications to these *Investment Beliefs* will occur if expectational, academic, experiential, historic, and/or statistical perspective suggests that a superior belief system exists.

INVESTMENT BELIEFS

1. Asset Class Decisions are Key

The Investment Management Division (IMD) believes that in general, decisions with respect to what asset classes and sub-asset classes to invest in, and the allocations to these asset classes and sub-asset classes, have a greater impact on total fund investment returns than decisions in which specific securities to invest.

2. Theories and Concepts should be Sound

IMD believes that over longer periods of time, investment outcomes (rates of return) conform to logical theories and concepts. We believe that significant deviations from theoretically and conceptually sound investment constructs (such as the internet bubble or the pre-subprime erosion of risk premiums) are usually not sustainable.

3. House Views should be Developed

IMD believes that the development and articulation of sound House Views (such as perspectives on interest rates, corporate spreads, and security pricing) will ensure consistency among investment decisions, clarity of investment direction, baselines for debates, and conformity of understanding.

4. Investment Strategies should be Forward Looking

IMD believes that investment strategies should be developed based upon forward looking insights (rather than simply successful strategies of the past).

5. Information Universes are Multiple

IMD believes that asset class valuations and security valuations are significantly affected by endogenous outcomes (such as earnings, GDP growth rates, and competitive barriers) that are probabilistic; and that these outcomes are typically analyzed well by the investment industry.

IMD believes that asset class valuations and security valuations are also significantly affected by random outcomes (such as natural disasters, and certain supply and demand shocks) that are virtually unpredictable; and that these outcomes are typically not analyzed directly by the investment industry.

IMD believes that asset class valuations and security valuations are also significantly affected by exogenous outcomes (such as foreign policies, and global cultural interactions) that can possibly be modeled; and that these outcomes are typically not analyzed by the investment industry.

6. Markets are Generally Informationally Efficient

Asset Class Valuations

IMD believes that asset class valuations (for instance stock market levels versus interest rate levels) are often in equilibrium with one another, but that anomalous situations do occur which result in disequilibria between asset class valuations. These disequilibria may offer valuable investment opportunities.

Security Valuations

IMD believes that security valuations (for instance IBM versus Cisco) are often in equilibrium with one another, but that anomalous situations do occur which result in disequilibria between security valuations. These disequilibria may offer valuable investment opportunities.

IMD believes that the extent of market informational efficiency varies across asset classes.

7. Market Frictions are Relevant

IMD believes that market frictions (such as including management fees, carried interest, revenue sharing, expenses, costs, transaction spreads, market impacts, taxes, and commissions) are known with greater certainty than expected returns and are significantly detrimental to investment performance.

IMD believes that investments and/or transactions should be initiated only to the extent that there is a strong level of conviction that they will result in increased investment returns or decreased risks net of market frictions.

8. Internal Investment Professionals are Beneficial

IMD believes that an in-house investment management operation that is engaged in internal portfolio management results in better investment decision making for the ASRS.

IMD believes that in-house investment personnel are more closely aligned with the purpose of the ASRS than most external parties.

IMD believes that in-house investment personnel have a greater understanding of the risk and reward tolerance of the ASRS than most external parties.

IMD believes that at the margin in-house investment personnel can impact direct investment negotiations with vendors, as well as influence investment industry conditions (such as private deal structures and public and private fee levels).

9. External Investment Management is Beneficial

IMD believes that external investment organizations can often offer greater expertise and/or greater resources and/or greater flexibility than internal personnel for various investment strategies.

10. Investment Consultants

IMD believes that investment consultants can and should be effectively utilized in the following four general categories, and that utilization of consultants should be focused on situations where there is a demonstrable need in at least one of the four areas:

- Independence: When ASRS' protocols or checks & balances can be enhanced
- Perspective: When ASRS' comparative understanding can be enhanced
- Special Skills: When IMD's skills can be enhanced
- Resource Allocation: When IMD's resources can be enhanced

11. Trustee Expertise

IMD believes that Trustees often have expertise in various areas of investment management and that this expertise should be utilized.

Caveat Statement

PERSONNEL & PROCESS CAPABILITY

The ASRS is somewhat limited in its ability to maintain or enhance IMD's capability due to state budgetary constraints, the state personnel classification system, the state procurement process, and state administrative processes.